costs (and make a contribution to fixed costs) for carriers to remain financially viable.[83]

Not only does Mr. Brock fail to include these sizable non-incremental costs in his "only 0.2 cents/minute" cost estimate, but he never explains why, contrary to the recommendation of the "experts" or the past decisions of this Commission, he thinks these legitimate costs should be excluded or why, of all network users, CMRS providers should be extended special treatment so that costs incurred on their behalf are subsidized by others.

Mr. Brock also makes in a second error: he mischaracterizes the scope and results of the so-called RAND Study. As Prof. Harris documents in Attachment A, Mr. Brock "misuses the results of a RAND Study to conclude that a LEC's cost of terminating traffic from a CMRS network is nearly zero."[84] Prof. Harris explains that, among other things, Mr. Brock:

- Did not take "significant incremental costs into consideration, including tandem-level switching and transport;"[85]
- Erroneously assumes that the incremental costs of switching in large urban exchanges in California using digital technologies are comparable to analog exchanges or the costs in suburban and rural exchanges;[86] and
- Engages in a methodology he criticizes elsewhere in his paper: averaging high peak costs over all minutes, from which he can obtain his "nearly

[83] Joint Brief of Petitioners AT&T Corp. and the Competitive Telecommunications Association, No. 94-70197 (9th Cir., filed Aug. 17, 1995)(internal citations omitted).

[84] Attachment A at 12.

[85] Id. at 13.

[86] Id. at 13-14.

> zero" estimate of $0.002 and then conclude that all interconnection — including at the peak hour — should be free.[87]

As Prof. Harris explains, "Dr. Brock's average cost estimate of $0.002 grossly understates the incremental cost of Type 2A interconnection services typically used by CMRS carriers. He excluded important incremental costs incurred by LECs to terminate CMRS minutes, he did not examine the high costs a LEC incurs with analog technologies or in non-urban exchanges, and he ignored altogether large classes of legitimate costs: common costs, overhead, and legacy costs. These omissions not only call into serious question his $0.002 cost estimate, but also call into serious question whether 'bill and keep' would be appropriate even under Dr. Brock's stated conditions."[88]

D. Adopting "Bill and Keep" Violates the Most Basic Principles of Economics

"The central tenet of economics is that prices play a critically important role in the allocation and distribution of goods and services in a market economy (hence the name of a key body of economics, 'price theory'). As a means of payment for the provision of services among competitors, 'bill and keep' . . . violates that principle."[89]

The use of "bill and keep" is without empirical foundation in a market economy. As Prof. Harris explains:

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[87] Id. at 14.

[88] Ibid.

[89] Prof. Harris, Attachment A at 4.

> In all of the industries I have studied, not once have I observed the equivalent of "bill and keep" arrangements: firms price the services they sell to each other to avoid the problems of bill and keep: opportunistic cost-avoidance, cost-shifting and cost-under-recovery. For these same reasons, "bill and keep" should not be employed as a means of "compensation" for interconnection services in telecommunications.[90]

Mr. Brock asserts that "bill and keep" is efficient because "each company has an incentive to increase the efficiency of its operations in order to reduce its costs," although he readily acknowledges this arrangement creates an incentive for carriers "to refuse to accept terminating traffic."[91] Mr. Brock is mistaken in claiming that "bill and keep" creates efficiency incentives. What it does is encourage carriers to shift as much of the cost of call termination onto the interconnecting carrier — which is precisely why carriers would become incented to refuse to accept terminating traffic.

Mr. Brock's contention that "bill and keep" gives LECs and CMRS providers the incentive to reduce their costs "makes no sense,"[92] as Prof. Harris explains:

> Requiring LECs to give away their services to CMRS carriers provides NO incentive for CMRS carriers to reduce the cost of terminating their customers' calls on the LEC's network. The whole point of setting prices at or above costs in a market economy is that people should pay for what they use. The

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[90] Attachment A at 6 (emphasis in original). Issues of compensation for transiting traffic — traffic originated by one carrier, transported by a second carrier, and terminated by a third carrier — make this clear. Traffic from a transiting carrier delivered to a terminating carrier will appear to the latter to have come from the transiting carrier and will be subject to the compensation charged to that type of carrier. If a carrier is allowed to interconnect under "bill and keep," there will be enormous incentives for other carriers (*e.g.*, IXCs) to connect to that carrier and deliver traffic to LECs through that carrier.

[91] Gerald W. Brock, Interconnection and Mutual Compensation With Partial Competition, at 13-14 (undated paper prepared for Comcast). *See also* Notice at 18 ¶ 34.

[92] Prof. Harris, Attachment A at 4.

"sender keep all" proposal is a transparent effort by cellular carriers to enjoy the benefits of an "in-kind exchange" of services of decidedly unequal value.[93]

For an "in-kind exchange" to be fair to both parties, the costs borne by each party must be at least roughly equivalent. This is certainly not the case with LEC-CMRS interconnection. For the foreseeable future, LECs will continue to serve the highest-cost landline customers. Hence, even if the volume of traffic exchange were equal (and we know it will not be), the cost of providing the ubiquitous network to terminate CMRS traffic will not be even remotely equal. Since CMRS providers and their subscribers benefit tremendously from the ability to make and receive calls from the millions of customers served by the PSTN, they should pay prices that cover incremental costs and contribute to the common costs of the PSTN.

E. The Supposed Advantages of "Bill and Keep" Lack Merit

The Notice recites several advantages of "bill and keep" touted by certain CMRS providers — advantages the Commission relies upon in tentatively concluding that "bill and keep" should be mandated for LEC-CMRS interconnection.[94] These advantages are illusory and certainly do not outweigh all the problems with "bill and keep."

CMRS providers first state that "bill and keep" would enable carriers to avoid the need to develop and maintain billing and accounting systems.[95] However, regardless of

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[93] Ibid. (emphasis in original).

[94] *See* Notice at 30 ¶¶ 61-62.

[95] *See* id. at 30 ¶ 61.

the compensation method used by carriers to exchange their traffic with each other, the fact remains that they need billing and accounting systems to charge their own subscribers. What is more, carriers need billing and accounting systems to record and bill usage of their networks for transit functions when, for example, a CMRS provider connects to an IXC through a LEC. Finally, LECs and many CMRS providers already have developed billing and accounting systems for their exchange of traffic, whether they bill the other for usage or to account for the flow of traffic. Consequently, the use of "bill and keep" will not permit carriers to avoid the development of billing and accounting systems.

Certain CMRS providers next assert that "bill and keep" would "prevent incumbent LECs that possess market power from charging excessively high interconnection rates."[96] To the extent there is a risk that a carrier will attempt to impose high rates to connect to its network, that risk applies to all carriers serving end users — including CMRS providers.[97] Free connection is certainly one way, *albeit* a very drastic way, of eliminating this risk.[98] But it is certainly not the only means of addressing the concern.

In assessing this risk of high interconnection charges, the Commission should draw upon the experience of the past, where LECs and CMRS providers have negotiated

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[96] Ibid.

[97] *See* Section V.B *infra* discussing the subject of "access bottlenecks."

[98] *See* Separate Statement of Commissioner Ness at 1-2 ("[a] strict regulatory prescription for an interconnection rate of zero represents a stronger exercise of regulatory power than is customary, even for pricing of LEC services.").

interconnections rates without intervention by regulators (and without complaint to regulators). That experience demonstrates, as U S WEST documented in Section I *supra,* that current interconnection charges are reasonable. Under no circumstances can they be characterized as "excessively high."

F. Adoption of "Bill and Keep" Would Constitute Poor Public Policy

The Commission has a long-standing policy that prices for telecommunications services should be based on costs.[99] Adoption of "bill and keep" would violate this fundamental policy. Even Mr. Brock, the strongest proponent for "bill and keep," readily acknowledges that this approach would result in "setting below-cost prices for terminating traffic."[100]

"Bill and keep's" departure from the Commission's cost-based pricing policies is alone grounds to reject it as a solution for LEC-CMRS interconnection, even for a temporary period of time. However, there are other public policy reasons on which to reject "bill and keep."

The Commission has noted that, as a matter of long-term policy, "the regulatory regime for interstate access charges should not vary dramatically from the rules relating to LEC-CMRS interconnection, to the extent that LEC-CMRS and LEC-IXC intercon-

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[99] *See, e.g.,* MTS and WATS Market Structure, CC Docket No. 78-72, Phase I, Third Report and Order, 93 FCC 2d 241 (1983); *modified on recon.*, 97 FCC 2d 682 (1983); *modified on further recon.*, 97 FCC 2d 834 (1984).

[100] *See* Notice at 18 ¶ 34.

nections use similar features and functions."[101] The Commission has correctly noted that carriers will engage in arbitrage if "substantially different prices [are imposed] for similar forms of interconnection."[102] If carriers like AT&T are able to obtain free interconnection for their CMRS traffic, they will have every incentive to route their non-CMRS traffic (*e.g.*, interexchange traffic) over their CMRS trunk groups.

U S WEST has already documented that CMRS providers enjoy very favorable interconnection charges *vis-à-vis* IXCs.[103] Giving CMRS providers free access will exacerbate considerably the existing disparity between CMRS and IXCs — thereby departing from the Commission's goal of uniform prices for uniform uses of the LEC network.

Giving CMRS providers free access would also represent very poor public policy. Even CMRS providers concede that LECs incur some costs in terminating CMRS traffic. They further acknowledge that traffic is not in balance. Consequently, if they are given free access, someone else must subsidize the cost of their free access.

The CMRS industry has not explained why it, of all industry segments, should be subsidized by others and be given protected status. CMRS providers, the Commission noted recently, charge "a significant premium" for their services and often earn

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[101] Id. at 9-10 ¶ 17.

[102] Id. at 37 ¶ 77.

[103] *See* Sectin I.B.2 *supra*.

"economic rents of significant proportions."[104] Given these facts, there is no basis whatever to require other network users to subsidize CMRS providers.

G. The LEC-LEC Precedent Cited by the CMRS Industry Does Not Support "Bill and Keep" for LEC-CMRS Interconnection

The CMRS industry cites two examples from LEC-LEC interconnection to support adoption of "bill and keep" for LEC-CMRS interconnection: (1) extended area service arrangements between incumbent LECs, and (2) the adoption by certain state commissions of "bill and keep" for interconnection between incumbent LECs and new LECs for an interim period of time. Neither example supports the use of "bill and keep" for LEC-CMRS interconnection, as U S WEST demonstrates below.

1. The EAS Compensation Model Is Inappropriate for Competitive Markets

CTIA has asserted that "bill and keep" is "a proven success . . . for over 100 years in the LEC world . . . . Applying such a policy for CMRS-to-LEC interconnection will stimulate the same kind of success as experienced LEC-to-LEC."[105] CTIA is wrong in assuming that a compensation mechanism developed in and for monopoly markets is appropriate for competitive markets.

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[104] Annual Report and Analysis of Competitive Market Conditions with Respect to Commercial Mobile Services, 10 FCC Rcd 8844, 8869 ¶ 75 and 8871 ¶ 81 (Aug. 18, 1995).

[105] Letter from Thomas E. Wheeler, CTIA, to Hon. Reed E. Hundt, FCC Chairman, at 1 (Nov. 20, 1995).

Telephone companies historically used "bill and keep" for extended area service ("EAS") arrangements. With EAS, one person may make a local call to another, even though the person being called is served by another (generally, neighboring) telephone company. "Bill and keep" was adopted for monopoly markets — that is, EAS participants were legally precluded from competing with each other for the same customer. In relying on this EAS compensation model, CTIA nowhere explains why this arrangement is appropriate for competitive markets.

Compensation arrangements between telephone companies had little significance in a monopoly franchise environment. Each telephone company was certificated by the same commission and subject to the same regulatory obligations and oversight. Each company generally served a comparable mix of business and residential customers, and each held the same universal service and carrier-of-last-resort obligations. In addition, while EAS traffic is often in relative balance, it was irrelevant in the end whether traffic was in balance.[106] With rate-of-return regulation, each telephone company was assured of being made whole for its costs through the revenue requirement, ratemaking, and separations process.

None of these considerations applies to competitive markets or CMRS providers. CMRS providers are not certificated by state commissions and are not subject to the same

[106] Evidence before the Washington Commission demonstrated that EAS traffic between incumbent LECs in that State was "in balance within ten percent." Fourth Supplemental Order, Docket No. UT-941464 *et al.*, at 36 (WUTC, Oct. 31, 1995).

regulatory obligations and oversight as landline LECs. Before enactment of the 1996 Telecommunications Act, CMRS providers had no explicit universal service obligations and still have no carrier-of-last-resort obligation. Moreover, there is no traffic balance between LECs and CMRS providers because of the premium pricing CMRS providers have chosen to use. Thus, even if the EAS model were appropriate for competitive markets, CMRS providers would not be eligible for "bill and keep" arrangements.

In fact, the EAS "bill and keep" model is singularly unsuited for application in a competitive environment. As the Washington Commission noted in holding that "bill and keep" was an inappropriate solution for incumbent LEC-new LEC interconnection, "competitive local exchange markets will require prices" because two LECs will not "likely . . . want or need exactly the same services, measured in either quantity or quality, from one another":

> [Prices are needed so] companies can both obtain the services they need from each other and receive the compensation that they deserve and require. With price tags attached to various interconnection services, LECs can choose and pay for the services that they need to satisfy their own customers.[107]

Indeed, the Washington Commission emphasized that prices were important even if traffic was in balance: "The structure and level of prices would affect companies' incentives and decisions in many areas, including investment in new capacity, retail rate structure, and marketing strategies."[108]

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[107] Fourth Supplemental Order, Docket No. UT-941464 *et al.*, at 31-32 (WUTC, Oct. 31, 1995).

[108] Id. at 30 n.12.

"Bill and keep" is inappropriate for another reason. Differences in traffic flows and costs were irrelevant in EAS because each incumbent LEC was assured of recovering any extra costs through the monopoly rate-of-return process. This major assumption is no longer accurate in a competitive environment in which incumbent LECs often operate under price-cap regulation. If an incumbent LEC incurs extra costs because of interconnection, those costs will now be flowed through to shareowners rather than to ratepayers. There is no law, at least in this country, which requires a private company to subsidize the services of its competitor.

2. The Washington PUC Order Adopting "Bill and Keep" for LEC-LEC Interconnection Is Not Precedent for Adopting "Bill and Keep" for LEC-CMRS Interconnection

The Notice references a recent decision of the Washington Utilities and Transportation Commission ("WUTC) ordering "bill and keep" as an interim compensation arrangement between landline LECs.[109] The Notice implies that this order is precedent for imposing "bill and keep" as the interim compensation arrangement for LEC-CMRS interconnections. This conclusion is erroneous; in fact, the WUTC order confirms that adoption of "bill and keep" for LEC-CMRS interconnection, even for an interim period, would be inappropriate.

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[109] *See* Notice at 13 ¶ 24. This Washington order was submitted by CTIA for the proposition that "bill and keep" was an appropriate compensation mechanism for LEC-CMRS interconnection. *See* Letter from Randall S. Coleman, CTIA, to John Nakahata, Legal Advisor to the Chairman, at 2 (Dec. 8, 1995). *See also* Notice at 19 ¶ 37.

Last fall, the WUTC adopted "bill and keep" as a temporary (nine-month) mechanism for compensating landline LECs for terminating each other's traffic, but only because it was "the least deficient of the alternatives offered in the record."[110] At the outset and as noted immediately above, the WUTC held that "bill and keep" was completely inappropriate as a final compensation arrangement among landline competitors because it "lacks the appropriate signals that are essential to an efficient competitive telecommunications market."[111]

Central to the WUTC's decision was its holding that "incumbents will not be financially harmed by adopting bill and keep on an interim basis."[112] The WUTC noted that incumbent and new LECs use "similar technologies," that new LECs would serve "the same community of interest area" (establishing the same local calling areas and rate centers as incumbent LECs), and that new LECs "should see calling characteristics that are highly similar to the dominant incumbent LEC."[113] Also of critical importance, the WUTC determined that "the only evidence on the record favors the theory that traffic [between landline LECs] will be close to balance."[114] In taking this interim step, the

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110 Fourth Supplemental Order, Docket No. UT-941464 *et al.*, at 29 (WUTC, Oct. 31, 1995). *See also* id. at 32 ("[W]e are not satisfied that the record here provides a basis to adopt any cost-based interconnection rates."). The WUTC further directed incumbent and new LECs to negotiate a replacement compensation arrangement and to submit their new plan for WUTC review within nine months. Id. at 33. In this regard, the WUTC stated that it would be "very surprised" if these negotiations resulted in a "bill and keep" structure. Id. at 31.

111 Id. at 31-32.

112 Ibid.

113 Id. at 29, 36, and 43.

114 Id. at 30. *See also* id. at 36 ("[T]raffic flows . . . are likely to be in balance.").

WUTC emphasized that it "would not [have] adopt[ed] bill and keep if it appeared that new entrant ALECs would be imposing more costs on the incumbents than they would be incurring by terminating incumbents' traffic."[115]

None of the reasons relied upon by the WUTC applies to the context of LEC-CMRS interconnection, and it is apparent that the WUTC would not have adopted "bill and keep" for such interconnections. First, the technical arrangements for LEC-CMRS interconnection are well established, and there is no need for incumbent LECs and new CMRS entrants to focus their efforts on those arrangements. Indeed, the compensation arrangements available to new CMRS entrants are also well established because CMRS providers — both incumbents and several new PCS licensees — have already negotiated them.

Second, unlike new entrant landline LECs, CMRS providers do not use similar technologies, do not serve the same community of interest area, and do not have calling characteristics that are highly similar to landline LECs. As a result, traffic between LECs and CMRS providers is not in balance, as the CMRS industry concedes and as the Commission acknowledges.[116] Industry data show that 70% of all CMRS traffic is mobile-to-land, while land-to-mobile calls account for only 25% (with the remaining 5% constituting mobile-to-mobile traffic).

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[115] Id. at 30.

[116] *See, e.g.*, Notice at 8 ¶ 14 ("LECs typically terminate many more calls that originate from the cellular network than an interconnecting cellular network terminates LEC-originated calls."). *See also* id. at 16 ¶ 29.

Third, incumbent LECs would be financially harmed if "bill and keep" were suddenly adopted for LEC-CMRS interconnection. Traffic imbalance between LECs and CMRS providers is a major reason for the harm. But this financial harm is also caused because that CMRS interconnection charges, unlike landline LEC-to-LEC charges, represent an existing revenue stream — a revenue stream which helps subsidize low rates for local residential service and a revenue stream that would be lost if this Commission were to impose "bill and keep."

In summary, the recent "bill and keep" LEC-LEC interconnection order entered by the Washington Commission does not support the adoption of "bill and keep" between LECs and CMRS providers. To the contrary, the reasons articulated by the Washington Commission suggest that it would have rejected "bill and keep" for LEC-CMRS interconnection.

H. Adoption of "Bill and Keep" Would Violate U S WEST's Constitutional Rights

As noted above, U S WEST generates substantial revenues from its CMRS interconnection charges — roughly 49¢ per month per residential customer. If the Commission were to adopt "bill and keep," even for an interim period, U S WEST would lose these revenues and have no opportunity to recoup them elsewhere. Indeed, since the LEC is the terminating carrier for an extremely high percentage of calls over a LEC-CMRS interconnection, "bill and keep" would afford it negligible revenues for providing this service. Requiring U S WEST to provide CMRS interconnection on a "bill and keep" basis would threaten to violate U S WEST's constitutional rights as guaranteed by the

Fifth Amendment to the United States Constitution. The fact that the Commission's order would work a taking makes it a presumptively unreasonable interpretation of the 1934 Communications Act and the 1996 Telecommunications Act.[117]

The Fifth Amendment provides that private property shall not be taken for public use without just compensation.[118] The U.S. Supreme Court recognized long ago that this right applies to and protects regulated companies:

> [The] power to regulate is not the power to destroy . . . . Under the pretense of regulating fares and freights, the State cannot require a railroad corporation to carry persons or property without reward; neither can it do that which in law amounts to a taking of private property for public use without just compensation, or without due process of law.[119]

Investors in public utilities have been induced to provide assets that serve the public by the promise of a fair return. Because utilities are particularly vulnerable to government takings, through the denial of that return after the assets are in place, the Supreme Court has provided regulated companies with greater protection under the Fifth Amendment:

> With regard to public utility regulation, a far different approach has been taken by the Court. There, constitutional principles are applied to prevent confiscatory regulation. Utilities are so vulnerable to arbitrary action of government, and the service utilities provide is so critical to the functioning of

[117] *See* Bell Atlantic Telephone v. FCC, 24 F.3d 1441, 1445 (D.C. Cir. 1994).

[118] U.S. Constitution, Amendment V.

[119] Stone v. Farmers' Loan & Trust Co., 116 U.S. 307, 331 (1886).

society as a whole, the courts have enforced a constitutional requirement designed to prevent confiscation of utility investment.[120]

Courts have long held that public utilities are constitutionally entitled to rates that will enable them to recover their costs in order "to operate successfully, to maintain [their] financial integrity, to attract capital, and to compensate their investors for the risks assumed."[121] In particular, requiring a telephone company to provide interconnection for negligible or inadequate compensation is a taking within the ambit of the Fifth Amendment.[122] To be sure, a rate order is unconstitutional on this ground only if its "overall effect" is confiscatory,[123] but that is precisely the case with an order to supply interconnection to CMRS on a "bill and keep" basis, which would flatly deny U S WEST historical and expected revenues without any offsetting increase elsewhere.

In this regard, the grant to CMRS providers of a continuous right of access to U S WEST's property — namely, its wires and switches — would also be the equivalent of a permanent physical occupation of that property.[124] Such a mandated physical occupation is, of course, a *per se* taking "without regard to whether the action achieves an important

[120] Richard McKenna, The Special Constitutional Status of Public Utility Regulation: From Munn to Duquesne Light, 21 U. West. L.A.L Rev. 31, 32 (1990). *See also* Richard McKenna and Ward W. Wueste, Jr., An Answer to Professor Pierce: How Utility Regulation Can be Reformed in Harmony with Constitutional Principles, 27 Cal. W. L. Rev. 81, 95 (1995).

[121] Federal Power Commission v. Hope Natural Gas Co., 320 U.S. 591, 605 (1944).

[122] *See, e.g.,* State v. Skagit River Telephone, 85 Wash. 625, 155 P. 144 (1916). *See also* Pacific Telephone v. Eshleman, 166 Cal. 640, 665-87, 137 P. 1119 (1913).

[123] *See* Duquene Light Co. v. Barasch, 488 U.S. 299 (1989).

[124] *See* Nollan v. California Coastal Comm'n, 483 U.S. 825, 831-32 (1987).

public benefit."[125] The D.C. Circuit has recently confirmed that the Commission cannot order physical takings of LEC property even to serve an important public purpose.[126]

Importantly, the interim nature of the proposed regulation does not diminish its effect as a taking. The Supreme Court has held that a temporary taking is no different than a permanent taking for which the Constitution indisputably requires compensation.[127] As that Court has stated, a government "may not transform private property into public property without compensation, even for [a] limited duration . . . . This is the very kind of thing that the Takings Clause of the Fifth Amendment was meant to prevent."[128]

The losses U S WEST would sustain through "bill and keep" are particularly harmful because U S WEST will never be able to recover them. Contrary to CTIA's as-

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[125] Loretto v. Teleprompter Manhattan CATV Corp., 458 U.S. 419, 434-35 (1982)(citations omitted).

[126] *See* Bell Atlantic Telephone v. FCC, 24 F.3d 1441, 1445 (D.C. Cir. 1994). Also irrelevant is the economic impact of the taking on the property owner, the Court holding that a physical occupation is a taking even if the occupation "has only minimal economic impact on the owner." Loretto, 458 U.S. at 434-35. Thus, completely baseless is CTIA's assertion that a public utility must prove that its property will be "rendered worthless" (*i.e.*, that it will receive no compensation) to establish a confiscation of its property." *See* Notice at 19 ¶ 37. As the Supreme Court has stated, "If the rate does not afford sufficient compensation, the State has taken the use of the utility property without paying just compensation." Duquesne Light v. Barasch, 488 U.S. 299, 616 (1989)(emphasis added).

Equally baseless is CTIA's assertion that public utilities may not recover profits. *See* Notice at 19 ¶ 37. The Supreme Court has recognized that utilities are entitled to a reasonable opportunity to recover not only their costs but a reasonable profit on their provision of service. "[W]hether a particular rate is 'unjust' or 'unreasonable' will depend to some extent on what is a fair rate of return given the risk under a particular rate-setting system, and on the amount of capital upon which the investors are entitled to earn that return." Duquesne Light, 488 U.S. at 310. Even if traffic exchange is equal, "bill and keep" provides no return on capital investments. Where traffic exchange is severely disparate, as it is between U S WEST and CMRS providers, U S WEST will actually lose money. Thus, this is not a case in which U S WEST will simply lose anticipated profits.

[127] *See, e.g.*, First English Evangelical Lutheran Church v. County of Los Angeles, 482 U.S. 304, 318 (1987)(unconstitutional taking under interim regulations required compensation).

[128] Webb's Fabulous Pharmacies v. Beckwith, 449 U.S. 155, 164 (1980).

sertion, U S WEST cannot "recover the costs for termination from its own end users in flat monthly charges."[129] Furthermore, the Commission's interim proposal provides no mechanism for adjusting U S WEST's intrastate rate base accounts to offset the heavy losses it would sustain by "bill and keep."

The revenues U S WEST receives from its CMRS interconnection charges are booked to intrastate accounts (because CMRS providers have not reported any interstate revenues). Under the Fifth Amendment, this Commission cannot diminish or eliminate this revenue stream without first finding other intrastate revenues to replace the loss U S WEST would sustain by "bill and keep." Even if new revenues were located, the fact that the Commission would be requiring U S WEST and its other customers to subsidize U S WEST's competitors by dedicating its property to its competitors' use at non-compensatory rates is of highly dubious constitutional validity.

III. PRICING PRINCIPLES FOR INTERCONNECTION NEGOTIATIONS

As discussed above, Section 252 dictates that, at least in the first instance, call termination interconnection arrangements among co-carriers be developed by negotiations. Section 252(d) further specifies that the test for determining the price of such call termination should be based on (but not limited to) the additional cost incurred by the carrier in accomplishing such termination. U S WEST below sets forth some of the fundamental principles which it believes should guide call termination pricing.

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[129] Notice at 19 ¶ 37. *See* Section II.A *supra*.

First, calculating the price/cost for call terminating services must be based on an understanding of network engineering and network capacity. As the Commission clearly understands, networks are engineered based on peak-usage times. A carrier seeking to reserve capacity for termination on U S WEST's network must reserve this capacity on a peak-usage basis, because U S WEST's network must be pre-engineered at the peak level. U S WEST must likewise reserve necessary capacity on the networks it wishes to terminate its subscribers' calls. If adequate capacity is not reserved, the originating network will find its terminating call attempts blocked by the terminating network.

Thus, the additional costs incurred in ensuring peak usage capacity availability for another's terminating traffic are the costs incurred by the terminating carrier in adding additional peak usage capacity. The costs incurred by the terminating carrier in engineering its network for the additional capacity demanded by originating carriers are real costs — and are not, as Mr. Brock suggests, costs which can be avoided simply by averaging them back into the existing network costs which were incurred in the course of engineering a network without the capacity for terminating the calls of the originating network at peak usage.

In short, a carrier seeking to terminate its traffic on the facilities of another network must reserve adequate capacity, and this reserved capacity should be set at peak usage levels (unless the network prefers to have its peak usage calls blocked).[130] The cost-

[130] In a competitive environment, each carrier must assume the responsibility for reserving sufficient capacity in other networks to terminate its traffic. Incumbent LECs in particular cannot be saddled with the

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based price of interconnection is assessed on the basis of capacity reservation. The price for capacity reservation would be established to represent the cost of service plus a reasonable profit.

Second, in addition to the price for capacity reservation, the network seeking call termination services will need to pay for network usage (both at the terminating end office and beyond). The most rational structure is to offer a tapered rate based on the capacity ordered. For calls made within the limit of the reserved channel capacity, the originating carrier would pay the terminating carrier the lowest available per-minute rate, representative of the average additional cost to terminate traffic on a properly engineered network. Arrangements for traffic beyond the reserved capacity would need to be negotiated; such calls would either be blocked or terminated with the originating carrier paying a higher, peak-load per-minute rate for this "out-of-bounds" traffic. The price for network usage would represent the additional cost to the network provider for call termination.

A third, longer-term principle which should guide call termination prices is the principle against cross subsidization.[131] Eventually, prices for call termination must be

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responsibility for forecasting the needs of other carriers, much less expend capital without a reasonable assurance that it will recover this investment (and make an adequate return).

[131] Of course, there are considerable subsidies built in the rates of incumbent LECs, whether by historical accident or by regulatory directive. A transition plan is therefore necessary before the non-subsidization principle can be fully implemented in the rates of incumbent LECs. The most important near-term objectives should be (a) to identify the subsidies so they become explicit, and (b) to fund the subsidies during the transition in a competitively neutral fashion.

set so that the customers of one network are not put in the position of subsidizing the services or customers of the other network. This can happen if the price is set too high or too low. If the terminating price is set too high, the customers of the originating network will subsidize the customers and services of the terminating network. Conversely, if the terminating price is set too low, the terminating carrier's customers will be put in the position of subsidizing the customers and services of the originating network. Neither of these scenarios would be satisfactory, reasonable, or lawful — certainly not if ordered by a governmental agency.

This non-subsidization principle would apply to the costs and prices of all interconnectors, not merely incumbent LECs. We do not suggest that this principle compels reliance on a single cost/price structure in determining the pricing mechanisms by which carriers charge others for termination. Indeed, insistence on such a uniform mechanism would be contrary to the Congressional preference for negotiation. However, to the extent the Commission chooses to become involved in setting costing or pricing rules for reciprocal carrier compensation for call termination, it must apply these rules uniformly and strictly avoid any scenario whereby one carrier, or class of carriers, is forced to require its own customers to subsidize similarly situated customers of the other carrier. Such a pricing scenario would be neither rational nor lawful.[132]

[132] The foregoing mechanism would apply equally to all entities seeking interconnection. However, additional price elements (*e.g.*, a flat rate to carriers to cover the existing carrier common line charge) will be necessary during a transition period to cover those groups of interconnectors and types of traffic required to pay an extra charge during the transition. Of course, the non-subsidization principle would not apply to universal service and high-cost support mechanisms.

IV. IMPLEMENTATION OF COMPENSATION ARRANGEMENTS

A. The Telecommunications Act of 1996 Moots the Commission's Tariff vs. Negotiations Inquiry

The Commission has tentatively concluded that it should have "some involvement in the formation and administration of [LEC-CMRS] interconnection arrangements," and it seeks "detailed comment on the type of involvement that would be optimal."[133] Among other things, it asks whether LECs should be required to file tariffs or, instead, disclose publicly privately negotiated interconnection agreements.[134]

This subject of procedures for interconnection, including LEC-CMRS interconnection, has been addressed in the Telecommunications Act of 1996, enacted after the Notice was released.[135] New Section 252 of the Communications Act expressly gives carriers, including incumbent LECs, the right to negotiate interconnection agreements.[136]

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[133] Notice at 42 ¶ 88.

[134] Id. at 44-45 ¶ 95.

[135] CTIA has recently taken the position, without citation to any authority, that the procedures set forth in new Section 252 do not apply to LEC-CMRS interconnection. *See* CTIA Comments and Opposition to Request for Extension, Docket No. 95-185, at 5 (Feb. 7, 1996). CTIA is wrong. As quoted above, the negotiation procedures set forth in Section 252 apply to any "telecommunications carrier." 47 U.S.C. § 252(a)(1). The term telecommunications carrier is defined broadly to include "any provider of telecommunications services, except that such term does not include aggregators of telecommunications services." 47 U.S.C. § 153(47)(emphasis added). The Joint Explanatory Statement of the Committee of Conference states that the statutory definition of 'telecommunications service' is sufficiently broad "to include commercial mobile service" (p. 114). There is, therefore, no basis whatever for CTIA's bald assertion that the Section 252 procedures do not apply to LEC-CMRS interconnection.

[136] New Section 252(f)(1) does give Bell companies the flexibility to file "statements" with state commissions if they choose. However, Section 252(f)(5) further specifies that state commission approval of such a statement "shall not relieve a Bell operating company of its duty to negotiate the terms and conditions of an agreement."

As noted above, Congress consciously rejected a provision in the final House of Representatives bill that would have required LECs to provide interconnection by means of general tariffs.[137]

Negotiated agreements must be submitted to the state commission for its approval to ensure that an agreement meets the requirements of the new Act and does not discriminate against carriers not a party to the agreement.[138] State commissions are also empowered to mediate and, in certain circumstances, arbitrate any disputes.[139] Section 252(e)(5) specifies that this Commission may become involved only "[i]f a State commission fails to act to carry out its responsibility under this section."[140]

Section 252(h) provides that the state commission "shall make a copy of each [interconnection] agreement . . . available for public inspection and copying." Section 252(i) provides that a local exchange carrier "shall make available any interconnection . . . provided under an agreement approved under this section to which it is a party to any other requesting telecommunications carrier upon the same terms and conditions as those provided in the agreement."

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[137] *See* H.R. 1555, § 244.

[138] *See* Section 252(e)(1) and (2).

[139] *See* Sections 252(a)(2), (b), (c), and (e).

[140] However, as explained elsewhere (*see* p. 28 and n.56), new Section 253(d) gives this Commission additional preemption authority in certain defined circumstances.

Although Section 252 gives primary responsibility to the state commissions to oversee interconnection agreements negotiated between LECs and other carriers, including CMRS providers, this Commission should find satisfaction that Congress adopted a procedure very similar to the good faith negotiation procedure the Commission developed almost a decade ago for interstate LEC-CMRS interconnection.

B. The Telecommunications Act of 1996 Also Moots the Issue of Preemption Relating to LEC-CMRS Interconnection

The Commission seeks comment on its tentative conclusion that it has "sufficient authority" to oust the States from continuing to regulate the rates LECs charge CMRS providers for interconnections pertaining to intrastate traffic.[141] This issue, too, has been mooted by the Telecommunications Act of 1996, which newly delineates the responsibilities of the States and the Federal Government with respect to interconnection.

Section 251 of the 1996 Act prescribes the responsibilities of LECs with respect to interconnection with other "telecommunications carriers" — a term broadly defined to include CMRS providers.[142] As discussed above, Section 252 establishes negotiation and arbitration procedures to implement those responsibilities and prescribes the standards for interconnection pricing. Section 252 charges the state commissions in the first instance with approving or rejecting negotiated agreements, or arbitrating interconnection dis-

[141] Notice at 53-54 ¶¶ 111 and 112.

[142] The 1996 Act defines a telecommunications carrier as "any provider of telecommunications services, except that such term does not include aggregators of telecommunications services." 47 U.S.C. § 153(49).

putes, subject to the provisions of Sections 251 and 252 and this Commission's implementation regulations. Section 252(e)(5) authorizes this Commission to preempt state jurisdiction "[i]f a State commission fails to act to carry out its responsibility under this section."

Obviously, there is no occasion at this early stage in the implementation of the 1996 Act for the Commission to consider exercising that preemption power with respect to CMRS interconnection.[143]

C. The 1993 Amendments to the Communications Act Do Not Give This Commission Exclusive Jurisdiction Over LEC-CMRS Interconnection Rates

For the first 60 years of the Communications Act of 1934, the line of demarcation separating federal jurisdiction from state jurisdiction was relatively bright: this Commission had exclusive jurisdiction over interstate and international traffic, but no jurisdiction over intrastate traffic — including the rates carriers charged each other for the exchange of intrastate traffic.[144] Indeed, the Commission repeatedly held that it had "no authority"

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[143] As discussed above, Section 253(d) does give this Commission to preempt state actions which "have the effect of prohibiting the ability of any entity to provide any interstate or intrastate telecommunications service." 47 U.S.C. § 253(a) and (d). However, given that U S WEST's interconnection charges represent less than 3% of a CMRS provider's revenues (*see* Section I.C.1 *supra*), it cannot credibly be claimed that current interconnection charges, negotiated in good faith, preclude CMRS providers from providing any service.

[144] *Compare* Section 2(a), which confers upon the FCC jurisdiction over "all interstate and foreign communication by wire or radio" *and* Section 2(b), which provides that "nothing in this Act shall be construed to apply or give the [FCC] jurisdiction with respect to (1) charges . . . or regulations for or in connection with intrastate communication service by wire or radio of any carrier." 47 U.S.C. § 152(a) and 152(b). *See generally* Louisiana Public Service Commission v. FCC, 476 U.S. 335, 370 (1986)(These provisions "define a national goal of the creation of a rapid and efficient phone service, and to enact a dual regulatory system to achieve that goal.").